

REBUTTAL TESTIMONY

OF

JUDITH R. MARSHALL

TELECOMMUNICATIONS DIVISION
ILLINOIS COMMERCE COMMISSION

ILLINOIS BELL TELEPHONE COMPANY
d/b/a AMERITECH ILLINOIS

DOCKET NO. 00-0700

MAY 11, 2001

ORIGINAL FILE

ALL. C. C. POINT NO. 000700

Staff 60

Date 6-28-01 Reporter CB

1 **Q. Please state your name and business address.**

2

3 A. My name is Judith R. Marshall and my business address is 527 East Capitol
4 Avenue, Springfield, Illinois 62701.

5

6 **Q. By whom are you employed and in what capacity?**

7

8 A. I am employed by the Illinois Commerce Commission ("Commission") as an
9 Economic Analyst in the Telecommunications Division.

10

11 **Q. Are you the same Judith R. Marshall that has previously offered pre-filed**
12 **testimony in this docket?**

13

14 A. Yes, I am. My direct testimony in this case is presented in ICC Staff Exhibit 2.0.

15

16 **Q. What is the purpose of your rebuttal testimony in this proceeding?**

17

18 A. My rebuttal testimony responds to the rebuttal testimony of Illinois Bell
19 Telephone Company d/b/a Ameritech Illinois ("AI" or "the Company") witness
20 Palmer. My testimony addresses the shared and common costs factors related
21 to this tariff.

22

23 **Q. Do any schedules and attachments accompany your testimony?**

24

25 A. Yes. Exhibit 6.0, Schedule 1, calculates the cumulative shared and common
26 costs factor under three scenarios described in the testimony that follows.
27 Attachment A is Ameritech's response to Data Request CLG 3.05. Attachment B
28 is a proprietary exhibit from Docket 97-0601/97-0602 which includes Ameritech
29 responses to AT&T data requests in that docket. Attachment C is Ameritech's
30 response to Data Request CLG 3.05. Each of these schedules and attachments
31 contains proprietary data.

32

33 **Q. Has your position regarding the Shared and Common Cost Factor changed**
34 **since the filing of your Direct Testimony in this docket?**

35

36 A. No, it has not.

37

38 **Q. Please summarize Mr. Palmer's response to the positions reflected in your**
39 **direct testimony.**

40

41 A. In summary, Mr. Palmer does not agree that this docket is an appropriate forum
42 for investigating the 1998 Shared and Common Costs Study. Changes to the
43 Shared and Common Costs Study impact all unbundled network elements
44 ("UNEs"). Mr. Palmer recommends that the Shared and Common Cost Model is
45 more appropriately addressed in a comprehensive proceeding addressing all of
46 the total element long run incremental cost ("TELRIC") studies filed in

47 compliance with the SBC/AI merger order. Mr. Palmer's testimony is described
48 more fully in the following rebuttal testimony.

49
50 **Q. Has AI provided any support for the shared and common costs factor that it**
51 **used in this case?**

52
53 **A.** No. The only mention of the shared and common costs factor used by AI is at
54 pages 5 and 6 of Mr. Palmer's rebuttal testimony where he states that the
55 Shared and Common Cost factor of % resulted from the Commission's Order
56 in Docket 96-0486/0569. In that Order, the Commission noted that on average
57 Ameritech Illinois' Shared and Common Cost Factor was 29%. (Order at 38).
58 The Commission also ordered other specific adjustments discussed in my direct
59 testimony which reduced AI's Shared and Common Costs. (Docket 96-0486, pp.
60 35-54 and Staff Exhibit 2.0, pp. 5-7). Absent any AI support of the % factor
61 other than the Order in Docket 96-0486, it appears that the Shared and Common
62 Cost Factor used by Mr. Palmer is unreasonably high and that an appropriate
63 factor based solely on that Order is less than 29%.

64
65 **Q. Is there other evidence that the factor utilized by Mr. Palmer is**
66 **unreasonably high?**

67
68 **A.** Yes, there is. Other states in the Ameritech region have recently investigated
69 Ameritech's calculation of its Shared and Common Costs Factor and determined

70 that a much lower Shared and Common Cost Factor is appropriate. For
71 example, Michigan found a Shared and Common Cost Factor of % and
72 Indiana found a Shared and Common Cost Factor of % to be appropriate.
73 The rate in Wisconsin is currently under investigation and the rate in Ohio
74 remains unchanged since its 1996 TELRIC case. (See Attachment A, AI
75 Response to Staff DR CLG 3.05.)
76

77 The Shared and Common Costs factors of other Ameritech states are relevant
78 because many common costs are allocated among the Ameritech regional
79 companies. The Commission recognized this in Docket 96-0486 when it
80 ordered that costs must be allocated to Illinois based on the extended TELRICs
81 for each state in the Ameritech region re-calculated using Illinois approved
82 TELRIC assumptions. (Order, Docket 96-0486, p. 54).
83

84 Similarly, In Docket 97-0601/0602 the Commission established a cap on Shared
85 and Common Costs associated with switched services of 28.86% for both
86 Ameritech and GTE. Ameritech agreed that the allocation of its shared and
87 common costs which produced the cap was reasonable. (Order, Docket 97-
88 0601-0602, p. 51). These comparisons demonstrate that Mr. Palmer's proposed
89 but unsupported Shared and Common Costs Factor of % is unreasonably
90 high and should not be utilized in this docket.
91

92 **Q. Did Mr. Palmer address the concerns with the Illinois 1998 Shared and**
93 **Common Cost Study which you identified in your direct testimony?**

94
95 A. No, Mr. Palmer did not address any of the specific concerns that I have with that
96 study. (Staff Ex. 2.0, pp.7-9). He only addresses whether this case is an
97 appropriate forum to investigate that study. (AI Ex. 2.1, p. 52).

98
99 **Q. Is it possible for Staff to simply adjust the Illinois 1998 Shared and**
100 **Common Costs Study to address your concerns?**

101
102 A. No, it is not. Some of the concerns included in my direct testimony require
103 information that is known only to Ameritech. Other concerns such as the use of
104 net present value ("NPV") calculations and current estimates of merger related
105 costs and savings should be able to be adjusted by Staff. However, when Staff
106 attempted to do sensitivity analyses using the model provided by Ameritech it
107 was unable to obtain anticipated results. In one scenario, Staff's adjustments
108 had no impact on the factor which indicates that Staff's adjustments were not
109 accepted by the model. In another scenario, significantly reduced shared and
110 common expenses produced the illogical result of increasing rather than
111 reducing the factor. Therefore, Staff has concluded that it cannot perform
112 sensitivity analyses using the model and procedures manual provided by
113 Ameritech.

115 **Q. Were you able to determine some of the reasons why Ameritech's Illinois**
116 **1998 Shared and Common Costs Model produced such flawed results?**

117

118 A. Yes, I determined that Ameritech's revised Shared and Common Costs model
119 failed to recognize any merger related net savings. This failure occurred
120 because the model utilized an inappropriate column which contains no merger
121 related net savings from Ameritech's supporting schedules. This flaw causes the
122 model to disregard any adjustment of the amount shown for net merger related
123 expense savings, since no merger related expense savings at all are reflected in
124 the study. The same flaw caused the illogical result of increasing the shared and
125 common cost factor by both ignoring changes to merger related net expense
126 savings in the numerator and recognizing changes to merger related net savings
127 reflected in the denominator.

128

129 **Q. What conclusions can you draw about Ameritech's Shared and Common**
130 **Costs Model from this flaw in the program?**

131

132 A. This flaw is significant. Ameritech's failure to detect this problem prior to
133 submitting the Illinois 1998 Shared and Common Costs Study leads me to two
134 conclusions. First, the program does not contain appropriate checks and
135 balances to assure logical results. It is relatively simple for a competent
136 computer programmer to include error messages to be displayed when an
137 illogical or opposite result occurs. It is also common for a computer program to

138 be designed to include a warning message when the user attempts changes
139 which will not be recognized by the program. In this case, Staff's attempted
140 changes were performed in accordance with the operating manual provided by
141 Ameritech. The manual does not state that such changes will not be recognized
142 by the program. Therefore, I conclude that Ameritech's Shared and Common
143 Cost model is defective.

144
145 Ameritech's failure to detect this significant flaw also leads me to conclude that
146 the model was not appropriately tested prior to its use. If Ameritech had
147 performed sensitivity analyses it should have obtained the same illogical results
148 as were obtained by Staff. Investigation of the illogical results would have
149 allowed Ameritech to identify this flaw and correct the computational errors in the
150 Illinois 1998 Shared and Common Costs Study prior to its submission to the
151 Commission. For these reasons, I conclude that neither the model nor the
152 Illinois 1998 Shared and Common Costs Study produced by this model should
153 be relied upon by the Commission.

154
155 **Q. Having identified this significant flaw in Ameritech's Illinois 1998 Shared**
156 **and Common Costs Study, were you able to adjust Ameritech's calculation**
157 **to correct this error?**

158
159 **A.** Yes. Exhibit 6.0, Schedule 1, page 1 of 3 corrects only the mathematical errors
160 in Ameritech's study. Correction of the errors, while still utilizing all Ameritech

assumptions, reduces the cumulative shared and common costs factor for
wholesale services from % to %.

Q. What information is shown on pages 2 and 3 of Exhibit 6.0, Schedule 1?

A. The information shown on pages 2 and 3 of Exhibit 6.0, Schedule 1 parallels the
calculation shown on page 1 of this schedule using alternative assumptions. In
my opinion, Ameritech's use of a net present value of merger related savings is
not forward looking in this third year of the study. The effect of removing the net
present value assumption to reflect year 2001 values (referred to as going level
values in the study) is shown on Exhibit 6.0, Schedule 1, page 2 of 3. This
calculation results in a cumulative shared and common costs factor of %

Finally, Exhibit 6.0, Schedule 1, page 3 of 3 calculates the result when current
estimates of net merger related savings are utilized. At least 96% of the current
estimate of net merger related savings are expected to be realized by 2002. In
my opinion, the use of year 2002 data where available is appropriately forward
looking and is most comparable to the preliminary budgeted data used in the
original TELRIC case, Docket 96-0486. The resulting cumulative shared and
common costs factor is %.

**Q. Do you recommend use of the cumulative shared and common costs factor
of %?**

184

185 A. I have provided the cumulative shared and common costs factor of % to Staff
186 witnesses Buckley and Liu for use in this case. As noted above, Staff does not
187 possess the necessary data to correct all of the flaws in Ameritech's Illinois 1998
188 Shared and Common Costs Study. In my opinion, Ameritech's proposed use of
189 a single, cumulative factor for the assignment of both shared and common costs
190 is not in compliance with the Commission's Order in Docket 96-0486. For these
191 reasons, the % factor should only be used on an interim basis until a forward
192 looking study that complies with prior Commission Orders can be completed. I
193 anticipate that a properly prepared shared and common cost study will produce
194 factors averaging less than % because Ameritech's operating expenses have
195 declined since 1998 while the demand for its services has increased.

196

197 **Q. Do you believe that Ameritech's use of a single cumulative factor for both**
198 **shared and common costs is in compliance with the Commission's TELRIC**
199 **Order in Docket 96-0486?**

200

201 A. No. The Commission's TELRIC Order finds:

202 "The methodology used for allocating shared and common
203 costs should be consistent for all network elements.
204 Ameritech Illinois should allocate shared and common costs
205 to unbundled loops based on specific extended TELRIC for
206 each rate zone, A, B, and C, thus developing total costs for
207 each element appropriately, i.e., based on the costs related
208 to the specific element.

209

210 We note Dr. Ankum's observation that Ameritech Illinois
211 allocates its shared and common costs across its five state

territories using extended TELRICS. This means the larger the Extended TELRIC, the larger the proportionate share of shared and common costs allocated to a given state. This will render the amount of shared and common costs allocated to Illinois dependent on the TELRICs approved in other jurisdictions. We will adopt Ms. Yow's suggestion to require that for purposes of allocation to Illinois, Ameritech Illinois shall use extended TELRICs based on the assumptions approved in Illinois.

Ameritech Illinois is directed to recalculate its rates based on the above adjustments."

(Order at 53). Clearly the extended TELRIC methodology is required by the original TELRIC Order.

The Commission's Order in Docket 96-0486 also distinguishes shared costs from common costs as follows:

"As Ameritech Illinois witness Broadhurst explained, Andersen developed a methodology for analyzing and attributing shared and common costs that it believed was consistent with the FCC Order. Andersen defined "shared costs" to be those costs incurred to provide two or more UNEs (including collocation and local transport and termination services) but which are unrelated to products and services that are not UNEs. It defined "common costs" to be those costs that are incurred to operate the business as a whole and are not directly associated with any individual UNEs, products or services or any groups thereof. Mr. Broadhurst states further that shared costs are synonymous with the term joint costs used by the FCC. (Al Ex. 4.0, p. 3)". (Order at 35).

"The Commission concludes that one aspect of Ameritech Illinois' allocation of common costs is unacceptable. The 1995 Ameritech Annual Report identifies a series of non-regulated, retail business activities under the title of "New Ventures." AT&T (Cross Ex. 4). Under Ameritech's allocation system, "New Ventures" improperly receives no allocation of common costs. New Ventures are "non-core" activities. Excluding New Ventures in the allocation process

253 decreased the ratio of "non-core" to "core" activities. If New
254 Ventures were added back, the core/non-core allocator
255 would decrease the amount of common costs eventually
256 allocated to unbundled network elements.
257

258 The exclusion of New Ventures means that none of the
259 President of Ameritech's salary, or the real estate costs, or
260 the costs of the Ameritech Institute are allocated to New
261 Ventures, even though all unbundled network elements will
262 bear part of these expenses. Ameritech Illinois is directed to
263 revise its calculations accordingly."
264

265 (Order at 51-52). Hence, shared costs must be assigned to one or more UNEs,
266 while common costs are to be spread over all of Ameritech's business
267 operations, including non-regulated activities and new ventures. Ameritech's use
268 of a single combined factor for both shared costs and common costs results in
269 the improper assignment of common costs to UNEs.
270

271 **Q. Is use of the extended TELRIC methodology significant to Ameritech's**
272 **allocation of shared and common costs?**
273

274 **A.** Yes, it is. The example which I have selected to demonstrate the significance of
275 using the extended TELRIC [or extended long run service incremental cost
276 ("LRSIC")] is a proprietary exhibit in Docket 97-0601 and 97-0602 which is
277 Attachment B to this testimony. In that docket, which dealt with access charges,
278 Ameritech also attempted to use an overall cumulative shared and common
279 costs factor of % rather than the Commission approved extended LRSIC
280 methodology. The exhibit demonstrates that the total shared and common costs
281 for switched services was only 28.8% using the extended LRSIC methodology

while the total shared and common costs for Billing and Collection were a whopping % using the extended LRSIC methodology. These significant differences in the factors for different services demonstrate the importance of proper application of the Commission's TELRIC Order to the allocation of shared and common costs. The Commission appropriately rejected Ameritech's use of the overall cumulative shared and common costs factor in Docket 97-0601 and 97-0602 and it should also reject it here.

Q. Did Ameritech supply the demand data which Staff requested in data request CLG 3.06 which you planned to address in this rebuttal testimony?

A. Ameritech provided only very limited current demand data related to loops. (See Attachment C, AI Response to DR CLG-3.06). That data is not sufficient to calculate the extended TELRIC methodology previously adopted by the Commission for the assignment of shared and common costs. However, the response clearly demonstrates the need for updated demand data because the figures for year 2000 "in-services quantities" of Loops (demand) significantly exceed 1997 forecasted demand for loops in all rate zones. The extended TELRIC methodology discussed above cannot be properly applied without complete demand data for both Illinois and the other Ameritech states.

303 Q. Are the issues identified in the Commission's Order initiating this
304 proceeding sufficiently broad to include a review of Ameritech's Shared
305 and Common Costs utilized in this tariff?

306
307 A. Yes. The Order initiating this docket states, "an investigation is initiated into
308 whether the rates and services for unbundled local switching with shared
309 transport provided by Illinois Bell Telephone Company pursuant to the tariff
310 pages are just and reasonable and in compliance with the provisions of law...".
311 (Order, Docket 00-0700, p. 2). Ameritech has the burden of proving that its
312 shared and common costs factor utilized in the development of this tariff is
313 reasonable. That burden cannot be met by putting off consideration of
314 Ameritech's cost models to some uncertain future date.

315
316 As Mr. Palmer stated, Issue No. 1 is "whether the costs and rates comply with
317 prior Commission and FCC Orders". (AI Ex. 2.1, pp. 52-53). As noted in my
318 testimony above, Ameritech has not demonstrated that its Shared and Common
319 Costs Factor complies with the Commission's Order in Docket 96-0486. The
320 % factor used is clearly in excess of the maximum cap for Ameritech Shared and
321 Common Costs established in Docket 97-0601/0602. Since compliance with
322 prior Commission Orders has not been demonstrated, a review of Ameritech's
323 Shared and Common Costs Study is appropriate.

326

327 **Q. Do you agree with Mr. Palmer's opinion that any update to Ameritech's**
328 **shared and common cost loading ultimately has an impact on the tariffed**
329 **prices for all of Ameritech's UNEs. (AI Exhibit 2.1, p. 53).**

330

331 **A. Absolutely. In Docket 98-0555 the Commission Ordered a mechanism for**
332 **sharing merger related savings with retail and wholesale customers through**
333 **updated cost studies and an allocation of savings between IXCs and end users.**
334 **(Order, Docket 98-0555 p. 140). We are now in the third calendar year since the**
335 **merger and Ameritech has avoided passing any merger related savings (which**
336 **are encompassed in the shared and common costs study) to purchasers of**
337 **UNEs. In my opinion, the tariffed prices for all of Ameritech's UNEs should be**
338 **adjusted when a current, forward-looking study of shared and common costs is**
339 **completed. This docket provides an appropriate forum for a Commission**
340 **conclusion regarding the shared and common costs study. Reductions of shared**
341 **and common costs ordered in this docket should affect the prices of all UNEs.**
342 **The Commission should not allow Ameritech to further delay the passing through**
343 **of merger savings or other cost decreases to all purchasers of UNEs.**

344

345 **Q. Do you agree with Mr. Palmer that each of the revised TELRIC cost studies**
346 **filed in compliance with the SBC/AI merger should be investigated? (AI**
347 **Exhibit 2.1, p. 54).**

348

349 A. No. The cost studies submitted in compliance with the SBC/AI merger are so
350 dated that they should no longer be considered forward-looking. Current,
351 forward looking cost studies should be submitted in support of any tariff change.
352 In the past, Staff has not devoted the resources to review cost studies outside of
353 a docketed case because we find that we are frequently unable to affect
354 changes in a company's cost studies absent a specific Commission Order.
355 Therefore, Staff looks at revised cost studies when they are used in a tariff filing
356 which can result in a specific Commission Order. If the Commission wishes
357 each of Ameritech's cost studies to be reviewed, I recommend that the Order in
358 this docket initiate a proceeding to address all Ameritech revised cost studies.

359

360 Q. **Please summarize your recommendations.**

361

362 A. The Commission should reject Ameritech's use of a cumulative shared and
363 common costs factor of % in this case. Staff's proposed cumulative shared
364 and common cost factor of % should be used on an interim basis until an
365 appropriate forward looking study of both shared costs and common costs is
366 completed. The Commission should order Ameritech to file revised tariffs for all
367 services reflecting the interim shared and common costs factor of % so that
368 merger related net savings are passed on to its customers.

369

370 The Commission should order Ameritech to perform a current study of shared
371 and common costs which is in full compliance with the Commission's prior orders

372 in Dockets 96-0486, 97-0601/0602, and 98-0555. In order to comply with these
373 orders, the study must distinguish between shared costs and common costs and
374 must utilize the extended TELRIC methodology. The study should also address
375 each of the concerns I have listed above and in my direct testimony. This study
376 should be forward looking and based on preliminary estimated budget data.

377
378 **Q. Does this conclude your rebuttal testimony?**

379
380 **A. Yes, it does.**
381
382

Docket No. 00-0700
Staff Schedule 2.1
Page 1 of 3
PUBLIC

AMERITCH ILLINOIS
SHARED AND COMMON COST FACTOR
(Dollars In Thousands)

Line No.

Description

Wholesale

Retail

THIS SCHEDULE CONTAINS PROPRIETARY DATA

Docket No. 00-0700
Staff Schedule 2.1
Page 2 of 3
PUBLIC

AMERITCH ILLINOIS
SHARED AND COMMON COST FACTOR
(Dollars In Thousands)

<u>Line No.</u>	<u>Description</u>	<u>Wholesale</u>	<u>Retail</u>
-----------------	--------------------	------------------	---------------

THIS SCHEDULE CONTAINS PROPRIETARY DATA

Docket No. 00-0700
Staff Schedule 2.1
Page 3 of 3
PUBLIC

AMERITCH ILLINOIS
SHARED AND COMMON COST FACTOR
(Dollars In Thousands)

<u>Line No.</u>	<u>Description</u>	<u>Wholesale</u>	<u>Retail</u>
-----------------	--------------------	------------------	---------------

THIS SCHEDULE CONTAINS PROPRIETARY DATA

Docket No. 00-0700
Staff Exhibit 6.0
Attachment A
PUBLIC

THIS ATTACHMENT CONTAINS PROPRIETARY DATA

Docket No. 00-0700
Staff Exhibit 6.0
Attachment B
PUBLIC

THIS ATTACHMENT CONTAINS PROPRIETARY DATA

Docket No. 00-0700
Staff Exhibit 6.0
Attachment C
PUBLIC

THIS ATTACHMENT CONTAINS PROPRIETARY DATA